Bourns Employees
Federal Credit Union

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April 23, 2015

Mr. Gerard Poliquin
Secretary to the NCUA Board
1775 Duke Street
Alexandria, VA 22314

Re: NCUA's Risk Based Capital Proposal, RIN 3133-AD77

Dear Mr. Poliquin

Bourns Employees Federal Credit Union (BEFCU) appreciates the opportunity to provide comments, including possible changes, regarding the National Credit Union Administration's (NCUA) proposed rule governing risk-based capital (RBC).

<u>Asset Size and the NCUA</u>
BEFCU has assets of less than $100 million; thus, the revised RBC proposal does not appear to apply. However, BEFCU's concern is that the NCUA will use the RBC proposal, including proposed risk weights, to exam the strengths, weaknesses, risks of credit unions with less than $100 million in assets. Thus, while not directly affected by RBC, there is a great apprehension that the NCUA will exam credit unions with less than $100 million in assets based on RBC and ultimately require, through the examination process, these credit unions to meet the RBC proposal.

<u>Smaller Credit Unions and Risk</u>
Another concern with RBC is the use of the $100 million in assets as a threshold for RBC. The $100 million threshold does not appear to have any significance or justification, except to eliminate compliance with RBC by a large number of smaller credit unions.

Based on prior experience as a CUSO president, I worked with a number of credit unions with less than $100 million in assets. Many of these credit unions had the same, and often times, more risk on their balance sheets and in their operations than credit unions with over $100 million in assets. Many of these credit unions:

- Offered, and retained on their balance sheets, some or all of the following products: real estate loans, business loans, participation loans, and/or indirect lending loans
- Offered internet banking, and/or other technology related services
- Supported growth with brokered certificates of deposit and/or share rates that exceeded competition.

Discussions with these smaller credit unions about their operations produced three reoccurring themes. First, if *we (as small credit unions)* do not offer products and services that the bigger credit unions do, our members will leave and *we* will (eventually) be forced to merge (not an outcome they wanted). Second, *we* need products that increase *our* income and capital (e.g., business loans, participation loans, and/or indirect lending). Third, *we* recognize we do not have the expertise we should but it is expensive and hard to attract based on *our* compensation structure. These same themes resonate today with many smaller credit unions.

Thus, while many under $100 million asset based credit unions are truly complex (i.e., by the products and services offered) this proposal ignores those credit unions; it leaves the NCUA to manage the risk of these smaller credit unions (which it can or will do through examination process).

<u>More Capital</u>
RBC introduces a different way to define risk and requires credit unions to have more capital to support that risk. This raises the following concerns.

1. There is little evidence to support the need for this change. Clearly a few credit unions failed during most recent recession; however, most credit unions survived and are in good shape. Those credit unions who failed generally were undercapitalized before the recession began (i.e., examination and net worth issues), had over valued assets (i.e., an examination issue, not a net worth issue), or chose to overlook or underestimate the risk they were taking (i.e., an examination issue).

2. The proposal appears to be more of a reaction than a common sense change (or it is a solution looking for a problem), while the recession affected many other financial institutions, credit unions fared quite well—and without the RBC proposal.

3. The proposal seems to be piloting or directing credit unions to a specific type of balance sheet structure through punitive risk weighting.

<u>Risk Weights (specific)</u>
With respect to specific risk weights, two categories, CUSOs and mortgage servicing, do not seem to be appropriately validated, vetted, and/or deliberated.

1. CUSO risk weighting appears to be heavily weighted based of a few failed CUSOs (e.g., the business lending CUSO that Telesis Community Credit Union had) and an assumption that CUSOs are inherently risky, regardless of products offered or their value proposition to credit unions.

   CUSOs that perform services only are important contributors to and factors for credit unions. They keep costs down, provide alternatives, and offer trusted assistance. Without these CUSOs, credit unions would pay more, have fewer choices, and be less competitive.

   NCUA should reevaluate and reconsider the risk weighting assigned to investments credit unions make in or loans credit unions make to CUSOs. Certainly, CUSOs who provide services have lower risk than CUSOs who originate and service business or mortgage loans.

2. The Mortgage Servicing weighting is the equivalent of telling credit unions not to sell mortgage loans, even if it benefits members.

a. For mortgage loans held in portfolio and are equal to or less than 35% of assets, RBC assigns a risk weight to those loans. If the mortgage loan portfolio exceeds 35% of assets, RBC assigns a higher risk weight to that portion of mortgage loans that exceed the 35% threshold.

   If a credit union chooses to sell and retain the servicing of mortgage loans that exceed the 35% threshold (and thereby avoid the higher risk weighting), RBC assigns a significantly higher risk weight to the Mortgage Servicing asset than to that portion of mortgage loans that exceed the 35% threshold.

   Thus, from a risk weighting perspective, it better to exceed the 35% of assets threshold than to sell loans and retain servicing.

b. The high-risk weighting assigned to Mortgage Servicing versus the lower risk weightings given mortgage loans over and under 35% of assets, gives the impression that it is better for credit unions to take interest rate risk than it is to sell loans and retain servicing. Intentional or not, RBC seems to overlook, discount, or not even be unaware of the 1980s savings and loan industry crisis: interest rates on savings products soared to 14%, 15%, and 16% while portfolio rates remained at 8%, 9%, and 10%—the negative spreads destroyed the industry.

c. Selling and retaining servicing of mortgage loans allows credit unions to off load credit and default risk while retaining their most valuable asset: the member! The Mortgage Servicing weighting inflicts a punitive result; it is excessive and it flies in the face of good balance sheet management and meeting member needs.

It is recommended that the Mortgage Servicing weighting be reduced to the same weighting assigned to mortgage loans held in portfolio and are under 35% of assets.

Finally, BEFCU suggests that the NCUA consider the cost, the time, the labor, the compliance requirements, and the technology needed to meet all of the changes RBC includes. The cost, compliance, and technology burdens credit unions have today are substantial; RBC will require many credit unions to redirect funds, staff, and other priorities to make and maintain changes in order to mitigate the effect of RBC on current operations.

Thank you very much for the opportunity to comment on this proposed regulation. The issues we discussed in this letter are a real concern to us. BEFCU hopes that the NCUA will share these concerns, take some additional time to review these areas, and make changes to the proposed rule.

If I can be of any assistance regarding this letter and the recommended changes, please contact me at edward.casanova@bourns.com or by phone at 951-781-5610.

Sincerely,

Ed Casanova

Edward Casanova
President and CEO
Bourns Employees Federal Credit Union